

Background

The Master Settlement Agreement

On November 23, 1998 the Kentucky Attorney General and other Attorneys General of 46 states, five U.S. territories and the District of Columbia reached an agreement with the four largest tobacco manufacturers (Brown & Williamson Tobacco Corporation, Lorillard Tobacco Company, Philip Morris Incorporated, R.J. Reynolds Tobacco Company), ending a four-year legal battle between the states and the tobacco industry that began in 1994. This agreement is known as the Master Settlement Agreement, or the MSA.

As a part of the MSA, the 46 states involved were awarded an estimated \$206 billion to be disbursed to the states beginning in 2000. Since the agreement did not dictate how states should spend the funds awarded in the settlement, it was incumbent upon each state legislature to decide how the funds would be used.

The Kentucky General Assembly passed legislation in 2000 which established how Kentucky's MSA funds would be allocated in the Commonwealth: 25% to be invested in early childhood development programs, 25% to be spent on tobacco cessation and research programs, and the remaining 50% to be devoted to agriculture. Subsequently, the General Assembly passed HB 611 which created the Agricultural Development Board to oversee investing the funds from the MSA.

Establishing Legislation

The General Assembly, with strong support from the Governor's Office, voted to invest 50% of Kentucky's MSA funds in the Rural Development Fund (KRS 248.655) also known as the Agricultural Development Fund (ADF). In an effort to ensure that tobacco dependent counties received a direct impact from the ADF, 35% of the ADF was allocated specifically to counties for county-level projects. One hundred and eighteen of Kentucky's one hundred and twenty counties receive a portion of the 35% county allocation. The specific funding level of a county is dependent upon its relative tobacco-production dependency to other counties in the state which is defined in KRS 248.703 (3).

The remaining 65% of the ADF is allocated for statewide projects, which includes several line item appropriations made each budget session by the Legislature. The funds remaining, after the line item appropriations have been taken out of the state funds, create the state grant pool used for statewide infrastructure investments in agriculture.

The Kentucky Agricultural Development Board (ADB) was established in KRS 248.707, as the entity that would administer the ADF. The Board serves to distribute both the county and state grant pool money in the ADF for the purpose of diversifying Kentucky's agricultural economy. This statute also identified the Governor's Office of Agricultural Policy (GOAP) as the entity that would provide administrative duties for the Kentucky ADB including all accounting, financial and grant transactions, research and policy recommendations.

Along with the establishment of an ADB, the Legislature identified the need for local, grassroots leadership in this historic investment; therefore, in KRS 248.721 County Councils were

established. These 8-member local county councils were created to provide local oversight to evaluate the needs of the local agricultural economy and devise a plan that would identify programs best suited for county agricultural development. They are to assist applicants in obtaining money from the ADF.

The Agricultural Development Board and Initial Policies

Governor Paul Patton appointed the first Agricultural Development Board in July 2000. With only the language in the statutes to guide them the Board and the staff of GOAP began working on developing the Board policies and procedures to administer and award the ADF. The initial meetings were focused on reviewing the legislation establishing the ADF and ADB, while structuring the initial development of the board. The ADB also reviewed and recommended a framework to assist the local county councils in developing their councils.

In September 2000, the ADB held a two-day meeting in Bowling Green and heard presentations from agricultural groups across the Commonwealth. At this meeting Governor Paul Patton presented the guiding principles he drafted for the Board to consider, and the Board adopted the principles. These principles set the tone and course of action for the Board for the following months and years. The ADB worked with a facilitator and GOAP staff to write the investment philosophy statement, and begin working on the Near-term Plan.

Also during this time, County Councils were required by statute to “devise a plan for the county that would identify programs best suited for the agricultural development of the county” (KRS 248.721). County Councils were encouraged to conduct planning meetings to create their county comprehensive plan for agriculture. GOAP staff served as an intermediary between the ADB and the 120 county councils, working with the counties in the development of the county plans, which were ultimately approved by the ADB.

The Near-term Investments

In December 2000, the ADB approved their Near-term Plan for Kentucky agriculture. In the plan they established general investment strategies and certain criteria for the near-term investment of the Agricultural Development Fund. The three general investment strategies that emerged from the Board’s deliberations and interactions with commodity and farm groups during this development process are:

- **Building the competitiveness of current selected agricultural sectors** that are already major or growing sectors of the current agricultural economy in Kentucky.
- **Support the development of new and emerging farm-based opportunities.** This area includes enterprise diversification efforts, related market development, technology development, entrepreneurial initiatives, and new cooperative ventures.
- **Develop local value-added processing of Kentucky agricultural products**—This includes helping producers explore the means to participate more directly in some of the value-adding activities.

The ADB also developed investment criteria, in an effort to provide some guidance and coordination of investment proposals that would come from different groups. The criteria were developed in keeping with the economic development objectives laid out in HB 611, with the goal of establishing broad categories from which near-term investments are most likely to achieve the HB 611 intended objectives. The criteria for prioritizing investments were:

- **Number of farmers involved**—investments that benefit more farmers will receive priority over more narrowly targeted projects. The level of investment required should be proportional to the number of producers benefiting or potentially benefiting.
- **Impact on net farm income**— investments that can demonstrate a high potential for directly increasing net farm income will receive priority. Projects that can lead to sustainable higher incomes for farmers are especially desired.
- **Impact on tobacco dependent communities**— HB 611 focuses considerable attention on developing projects that can help tobacco farmers and communities dependent on tobacco income to develop additional enterprises.
- **Potential for clustered activity**— given limited resources and the need to ensure success of state-wide programs, the Agricultural Development Board is especially interested in projects that can be developed on a pilot basis in a geographic area and then expanded as impacts from the pilot investment become more certain. Such projects will ideally be initially developed in areas that exhibit the greatest chance for success.
- **Time Frame**— investments with long periods before generating positive returns or involve greater risk need to generate relatively greater benefits to offset the deferred or riskier payoffs.
- **Growth potential**— investments that can demonstrate relatively higher growth potential, both in terms of return per producers and in terms of number of producers benefiting, will be more aggressively pursued. Projects may need to take into account a longer planning range to demonstrate when and how significant growth may occur.

With these strategies and criteria the ADB recognized that implicit in the support of each of these areas is the assembly of appropriate technical support, developing grower and business leadership, and expanding the institutional support necessary to ensure sustainable benefits to the agricultural community and Kentucky. As such, the GOAP staff began working with the Universities, the Small Business Development Centers, and other organizations to provide the support that would be needed by producers, organizations, and businesses to produce competitive and viable proposals.

The Application Process

The Near-term Plan also established the implementation responsibilities of the staff, ADB, and County Councils for the grant application process. The plan established that the Board will distribute application forms and conduct an aggressive communications campaign to ensure the highest possible level of public awareness of the availability of opportunities from the Agricultural Development Fund. The agricultural development councils located in each county shall be responsible for raising public awareness of this plan in their communities. The councils shall also work with area farmers to clarify their understanding of the application and evaluation process and provide direction when needed on the development of project proposals.

In January 2001, ADF grant applications were distributed across the Commonwealth. The application focused heavily on the criteria outlined in the Near-term Plan, with a focus on business plan and development. This standard application form was utilized by all applicants, regardless of size or ownership status.

By intention and design, the UK Cooperative Extension Service has played a significant role in the implementation and support of the programs administered by the ADB. County Extension Agents for Agriculture and Natural Resources have performed many duties aimed at assisting producers with the ADF application forms, organizing County Councils, and information dissemination. In many cases, County Agents have served a role similar to an executive secretary or administrator by assisting in the functions of county councils, organizing meetings, working directly with producers, and handling paperwork. Agents have worked with the councils to develop comprehensive plans by supplying statistical data and providing clerical assistance and have provided various forms of assistance to county program administrators. Agents have provided feedback to the ADB regarding the function of programs and provide opportunities for producers to comply with required training. Contributions of county agents were especially important to the most rural participants, e.g. directly with producers to provide them with necessary forms, information, and assistance with paperwork required for the various county programs. UK Extension faculty and specialists were also involved from the inception of the ADF, providing science-based information to the GOAP regarding program specifics and training for producers involved in the various programs.

County Councils were given the responsibility of ensuring that all proposals for county funds receive appropriate evaluation, using the County Plans as an investment guide. The ADB and GOAP staff received and evaluated all proposals for state funds. Yet, the ADB maintained ultimate authority and accountability for the use of both state and county funds, which meant that all county investments had to also be reviewed and approved by the ADB. In early 2001, the staff and ADB began receiving and reviewing a wide array of applications from individuals and organizations across the Commonwealth.

The County Model Programs

As staff reviewed the applications in early 2001, they began to identify a trend in several county level applications. These applications were requesting funds for improvements on individual farms.

In an effort to accommodate county councils that identified these on-farm improvements as essential to agricultural development, the GOAP – along with staff from the Kentucky Department of Agriculture, UK College of Agriculture, industry organizations, and local councils – worked to develop Model Programs.

Model programs were designed to improve the efficiency and decrease the bureaucracy of funding county-level projects for individual on-farm improvements with county funds. These programs had a secondary benefit of empowering local organizations to become leaders by administering the programs.

Also, in response to a need of consistency and funding standards across the counties, the ADB chose to set state guidelines and eligible investment items within the model programs. All the

model programs were designed to provide 50% of the cost of the project to the qualified program participants.

The first model program introduced and funded in March 2001 was the Cattle Genetics Improvement program. This program, like all the model programs, came from a local county application and was developed into a statewide initiative. Since the creation of this first model program, staff has worked with agricultural organizations across the Commonwealth to develop additional model programs originating from requests from the counties. County councils and farmers continue to find the various model programs extremely popular and an excellent method to get funds in the hands of farmers.

Project Analysis by the GOAP Staff

Since the beginning of the application process, the GOAP staff has been closely involved with project analysis and communication from the moment an application enters the office, until the final report is submitted by an award recipient. In the beginning, as an application arrived in the office, it was assigned to a staffer. Eventually Project Analyst (PA) positions were created to serve as a liaison between the County Councils and the GOAP, plus serve as a liaison between the applicant and the ADB.

PAs play a critical role in the project evaluation process. They meet each week to review, in detail, projects under consideration for the upcoming ADB meeting. PAs review project applications and work with the applicant to ensure that the business plan, financial information and other issues related to the proposed project are addressed. They provide an analysis of applications to the ADB and answer members' questions. Plus, they work with the GOAP attorney to develop the terms and conditions under which the project would be funded.

The First Funding

In March 2001, the first projects were approved for funding by the ADB. The state level projects receiving funds in this first approval were cooperative-based organizations, such as Western Kentucky Growers Cooperative, that had a large farmer membership. The county level projects approved included a mix of educational based initiatives, local county farm organizations, and entities that had submitted requests that fit into the Cattle Genetics model program. The projects funded in that first month set a precedent for the type of projects to be approved in the ADF's early years.

Long Term Planning

During the establishment of the application process and the review of early applications, GOAP continued to move forward with developing a long-term plan. With a foundation of the Near-term Plan and the county plans, GOAP staff began the monumental task of creating a long-term plan for Kentucky agriculture. Staff conducted 14 regional meetings across the state and a two-day summit involving over 700 agricultural and policy leaders from around the state and nation

including: farmers, religious and civic leaders, educators, business people, and medical professionals. Participants in these sessions were encouraged to think across county lines, while identifying the most important issues related to long-term agricultural economic development in their regions.

GOAP Staff took the 120 county plans and the notes from the sessions and compiled a draft in the Fall of 2001. GOAP conducted another series of regional meetings to share the draft with the people who would be most directly impacted by the implementation of this plan. As a result of these feedback forums, the plan was modified. After 18 months in the making, Cultivating Rural Prosperity: Kentucky's Long-Term Plan for Agriculture was approved by the Agricultural Development Board in January 2002 and introduced to the public in March 2002. The plan addresses areas of investment concentration and activities to be successfully completed under the guidance of the ADB.

Cultivating Rural Prosperity identifies marketing and market development as Kentucky's number one priority. Therefore the ADB, in February 2002, committed 50% of the biennium's remaining state funds to this effort. The second priority identified in the Plan was access to capital. To move this initiative forward, the ADB passed a resolution in January 2002 supporting the re-activation of the Kentucky Agricultural Finance Corporation (KAFC) for the dual purpose of expanding farmer access to capital and focusing on value-added processing projects. The other priorities identified in the Long-term Plan include:

- Providing financial incentives for sound environmental practices,
- Improving educational opportunities for farm families,
- Committing to the further development of local leadership, and
- Expanding Kentucky's agricultural research and development capacity

This plan was recognized as the first plan in Kentucky's history where local agricultural development councils in every county of the Commonwealth facilitated public discussions about the future of agriculture in their communities.

Oversight Committee

In KRS 248.723, a permanent subcommittee of the Legislative Research Commission to be known as the Tobacco Settlement Agreement Fund Oversight Committee (TSAFOC) was established. This twelve member committee, consisting of six House members and six Senate members, was established to review the monthly funding decisions made by the ADB during the previous month's meeting. In reviewing the projects, the subcommittee is directed to determine whether the criteria or requirements of House Bill 611 are met and whether any other requirements have been met. If the subcommittee determines that any of the criteria have not been met, then the subcommittee may, by majority vote, recommend to the ADB in writing that a project not be approved. If the subcommittee determines that all relevant criteria are met by any proposal, then they may, by majority vote, recommend to the ADB in writing that the project be approved.

The first meeting of the TSAFOC was not held until May of 2003, due to the Senate's delay in appointing members to the committee. By that time the guiding principles, investment policy,

application process, long-term plan, county model programs, and over two years of projects had been approved by the ADB.

The Annual Review

When the ADB approved the Long-term Plan in January of 2002 they recognized that the plan was a living document that should continue to be evaluated by the ADB to assess its applicability. As such in October 2003, the ADB conducted the first annual planning session to assess the application process and investment decisions made since the first grant was funded in March 2001. At this meeting ADB members suggested various recommendations for change of their application review process that would help in their due diligence of important investment decisions and better fund management. This annual evaluation of funded projects, programs, and investment focus continues today.

Evaluation Methodology

Evaluation Design

As agreed in discussions with ADB members and GOAP staff, the overall goal of this evaluation is to assess the effectiveness of the ADB investments in agriculture, agribusiness, and leadership development over 2001-2006 by systematically examining outcomes and impacts of selected activities: State Non-Model Projects, County Non-Model and Model Programs, and the Kentucky Agricultural Finance Corporation.

The ADB's stated overall goal is presented on the GOAP webpage:

The Board will invest these funds in innovative proposals that increase net farm income and effect tobacco farmers, tobacco-impacted communities and agriculture across the state by stimulating markets for Kentucky agricultural products, finding new ways to add value to Kentucky agricultural products, and exploring new opportunities for Kentucky farms.

Overall effectiveness is evaluated in this study relative to this general goal plus specific goals related to Non-Model Projects, the Model Program funding, and the funds transferred to the KAFC. The evaluation criteria for each of these are outlined in the major sections of this report.

In addition, the ADB and GOAP staff also requested that the evaluation examine four key questions relative to the impact of the ADB investments:

1. Where would Kentucky's agriculture be without the ADB investments?
2. What have been the quantitative and qualitative impacts of ADB expenditures?
3. How have ADB investments leveraged other resources?
4. How have ADB programs affected county leadership and entrepreneurial leadership?

To conduct this evaluation, UK proposed a collaborative approach in which the staff of GOAP and members of the ADB will be involved with the UK Team in providing data and information, adapting a LOGIC model to fit the unique set of investments being examined (Non-Model, Model, or KAFC loans), and participating in site visits and interviews. The UK Team took responsibility for the data collection, the general survey instruments, site visits and interviews, expert group consultations, and the impact analysis. To assist in analyzing impacts and consequences, the UK Team sought assistance from other UK faculty, County Agents for Agriculture and Natural Resources, consultants, and other individuals with experience or expertise in specific areas. However, all judgments and conclusions are the responsibility of the UK Team.

LOGIC Model Framework

To guide the overall evaluation effort, the UK Team developed a modified Logic model (summarized below) to provide the framework for linking the overall investment goal to the project investments (the inputs) and, logically, to the outputs and impacts.

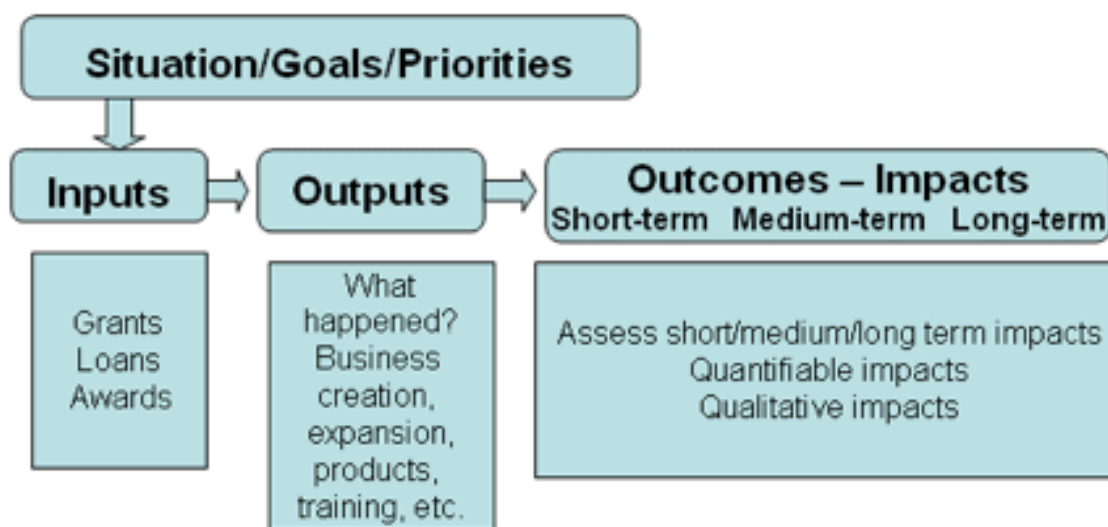


Figure 1: LOGIC Model.

Since ADB investments began in 2001, it was anticipated that most of the impacts would be short and medium-term. However, judgments were rendered in cases where potential for long-term impacts seemed likely.

The evaluation was initiated by focusing on the large and medium investments in the Non-Model Program, which represent a majority of the invested funds but a fraction of the total number of projects. The UK Team identified a stratified, representative sample of the “small” category investments and the county non-model investments to analyze the numerous smaller non-model projects.

Evaluation of the County Model Programs was directed by the Assistant Extension Director for Agriculture and Natural Resources in the UK College of Agriculture.

The UK Team approached the evaluation of the loans implemented by the KAFC with ADB funding using the same basic conceptual approach as with the Non-Model Program. A stratified sample of the KAFC loan portfolio was identified for all agricultural infrastructure and Beginning Farmer loans. In addition, the UK Team visited all three Coordinated Value-Added loan recipients and the single Agricultural Processing loan.